

CITY OF COTTONWOOD FALLS  
CHASE COUNTY, KANSAS  
INDEPENDENT AUDITORS' REPORT AND  
STATUTORY BASIS FINANCIAL STATEMENTS  
YEAR ENDED DECEMBER 31, 2011

ALDRICH AND COMPANY LLC  
CERTIFIED PUBLIC ACCOUNTANTS  
COUNCIL GROVE, KANSAS 66846

City of Cottonwood Falls  
Chase County, Kansas

STATUTORY BASIS FINANCIAL STATEMENTS  
Year Ended December 31, 2011

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# ALDRICH & COMPANY, LLC

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CERTIFIED PUBLIC ACCOUNTANTS

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## Independent Auditors' Report

Mayor and City Council  
City of Cottonwood Falls, Kansas

We have audited the accompanying primary government financial statements of the City of Cottonwood Falls, Kansas, as of and for the year ended December 31, 2011, as listed in the table of contents. These statutory basis financial statements are the responsibility of City of Cottonwood Falls, Kansas, management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the guidance in the Kansas Municipal Audit Guide. Those standards and guidance require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

The primary government financial statements referred to above do not include the financial data of component units of the City of Cottonwood Falls, Kansas, as of December 31, 2011. Accounting principles generally accepted in the United States of America require the financial data of the City's component units to be reported with the financial data of the City, unless separate financial statements are also issued for the component unit. The city has not issued such financial statements. The effect on the primary government financial statements of the omission of the component units, although not reasonably determinable, is presumed to be material.

As described in Note 1, the City of Cottonwood Falls, Kansas, prepared these financial statements in conformity with the accounting practices prescribed by the State of Kansas to demonstrate compliance with the cash basis and budget laws of the State of Kansas, which practices differ from accounting principles generally accepted in the United States of America. The effects on the financial statements of differences between these regulatory practices and accounting principles generally accepted in the United States of America, although not reasonably determinable, are presumed to be material.

As described in Note 1, the city uses various types of funds to account for the operations of the city. The separate funds are used to account for specific activities of the city. The city has not reasonably allocated the expenses of the city in respect to its general and proprietary funds. Additionally, supporting documentation was not available to substantiate the validity all of the city's disbursements, and were therefore considered misstatements. These misclassifications and misstatements are considered to be material to the financial statements taken as a whole.

In our opinion, because of the omission of the discretely presented component units, as discussed above, and because of the effects of the matters discussed in the preceding two paragraphs, the financial statements do not present fairly, in conformity with accounting principles generally accepted in the United States of America, the financial position of the City of Cottonwood Falls, Kansas, as of December 31, 2011, or the changes in its financial position, or where applicable, its cash flows for the year then ended.

Also, in our opinion, because of the effects of the matter discussed in the paragraph above regarding fund misclassifications and misstatements, the statutory basis financial statements referred to above do not present fairly, in all material respects, the cash and unencumbered cash balances of the primary government of the City of Cottonwood Falls, Kansas, as of December 31, 2011, and its cash receipts and expenditures and budgetary results, for the year then ended, taken as a whole, on the basis of accounting described in Note 1.

*Aldrich & Company, LLC*

Aldrich & Company, LLC  
August 1, 2012

City of Cottonwood Falls  
Chase County, Kansas

Statement 1

Summary of Cash Receipts, Expenditures, and Unencumbered Cash  
For the Year Ended December 31, 2011

Fund	Beginning Unencumbered Cash Balance	Cash Receipts	Expenditures	Ending Unencumbered Cash Balance	Add Outstanding Encumbrances and Accounts Payable	Ending Cash Balance
General Fund	\$ 17,936	\$ 415,248	\$ 372,326	\$ 60,858	\$ 16,234	\$ 77,092
Special Revenue Funds						
Sales Tax Fund	98,389	78,968	69,928	107,429	0	107,429
Special Highway	39,793	23,213	20,209	42,797	0	42,797
Special Parks & Recreation	1,055	1,699	726	2,028	207	2,235
Municipal Equipment Reserve	74,286	11,667	63,932	22,021	0	22,021
Swope Park Equipment	7,376	0	0	7,376	0	7,376
Streetscape	5,730	206	350	5,586	0	5,586
Community Building Equipment	97	0	12	85	0	85
Veterans Memorial	8,780	755	8	9,527	0	9,527
Cottonwood Falls Volunteers	80	0	0	80	0	80
Debt Service Funds						
Bond and Interest	16,655	20,360	16,317	20,698	0	20,698
Proprietary Funds						
Sewer Fund	45,682	44,535	47,203	43,014	279	43,293
Solid Waste Fund	36,623	95,199	102,388	29,434	7,691	37,125
Water Fund	22,724	163,889	194,163	(7,550)	9,342	1,792
Total Reporting Entity (Excluding Agency Funds)	<u>\$ 375,206</u>	<u>\$ 855,739</u>	<u>\$ 887,562</u>	<u>\$ 343,383</u>	<u>\$ 33,753</u>	<u>\$ 377,136</u>

Composition of Cash:

Checking	\$ 82,884
Certificates of Deposit	301,170
Petty cash - City Clerk	150
	<u>384,204</u>
Less: Agency Funds per Statement 4	(7,068)
Total Reporting Entity (Excluding Agency Funds)	<u>\$ 377,136</u>

The accompanying notes are an integral part of this statement.

City of Cottonwood Falls  
Chase County, Kansas

Statement 2

Summary of Expenditures – Actual and Budget  
For the Year Ended December 31, 2011

FUNDS	Certified Budget	Adjustment for Qualifying Budget Credits	Total Budget for Comparison	Expenditures Chargeable to Current Year	Variance Favorable (Unfavorable)
General Fund	\$ 549,610	\$ 0	\$ 549,610	\$ 372,326	\$ 177,284
Special Revenue Funds					
Sales Tax	195,996	0	195,996	69,928	126,068
Special Highway	113,049	0	113,049	20,209	92,840
Special Parks & Recreation	3,975	0	3,975	726	3,249
Debt Service Funds					
Bond and Interest Fund	37,076	0	37,076	16,317	20,759
Enterprise Funds					
Sewer Fund	94,411	0	94,411	47,203	47,208
Solid Waste Fund	112,267	0	112,267	102,388	9,879
Water Fund	192,779	0	192,779	194,163	(1,384)

The accompanying notes are an integral part of this statement.

City of Cottonwood Falls  
Chase County, Kansas

Statement 3-1

GENERAL FUND  
Statement of Cash Receipts and Expenditures – Actual and Budget  
For the Year Ended December 31, 2011

	Current Year		Variance
	Actual	Budget	Favorable (Unfavorable)
Cash Receipts			
County Tax	\$ 322,097	\$ 319,172	\$ 2,925
Liquor Tax	1,699	1,657	42
Community Building Rent	2,700	2,550	150
Court Fees	297	2,500	(2,203)
Franchise Fees	44,134	42,000	2,134
Interest on Idle Funds	3,140	9,700	(6,560)
Licenses and Permits	530	250	280
Miscellaneous	14,849	11,300	3,549
Municipal Building Rental	3,879	4,500	(621)
Park Rental	1,598	2,500	(902)
Street	0	22	(22)
Swimming Pool	20,325	17,850	2,475
Total Cash Receipts	415,248	414,001	1,247
Expenditures			
General Government			
Personal	56,398	50,770	(5,628)
Contractual	43,135	37,880	(5,255)
Commodities	17,270	12,950	(4,320)
Shop Expense	15,430	8,030	(7,400)
Uniforms	3,546	2,220	(1,326)
Total General Government	135,779	111,850	(23,929)
Streets	25,369	56,020	30,651
Airport	652	1,990	1,338
Pool	36,472	44,290	7,818
Parks	23,331	21,505	(1,826)
Public Safety	20,616	26,425	5,809
Employee Benefits	51,876	43,330	(8,546)
Law Enforcement	9,000	9,575	575
Housing Authority	10,313	10,185	(128)
Industrial Development	4,000	4,245	245
Noxious Weed	2,750	105	(2,645)
Dump	2,081	0	(2,081)
Capital Outlay	38,420	180,090	141,670
Operating Transfers	11,667	40,000	28,333
Total Expenditures and Transfers Subject to Budget	372,326	549,610	177,284
Receipts Over (Under) Expenditures	42,922	\$ (135,609)	\$ 178,531
Unencumbered Cash, January 1	17,936		
Unencumbered Cash, December 31	\$ 60,858		

The accompanying notes are an integral part of this statement.

City of Cottonwood Falls  
Chase County, Kansas

Statement 3-2

SPECIAL REVENUE FUND  
Statement of Cash Receipts and Expenditures – Actual and Budget  
For the Year Ended December 31, 2011

SALES TAX FUND

	Current Year		Variance Favorable (Unfavorable)
	Actual	Budget	
Cash Receipts			
Sales Tax	\$ 78,968	\$ 66,000	\$ 12,968
Total Cash Receipts	78,968	66,000	12,968
Expenditures			
Capital outlay	69,928	195,996	126,068
Total Expenditures	69,928	195,996	126,068
Receipts Over (Under) Expenditures	9,040	\$ (129,996)	\$ 139,036
Unencumbered Cash, January 1	98,389		
Unencumbered Cash, December 31	\$ 107,429		

The accompanying notes are an integral part of this statement.

City of Cottonwood Falls  
Chase County, Kansas

Statement 3-3

SPECIAL REVENUE FUND  
Statement of Cash Receipts and Expenditures – Actual and Budget  
For the Year Ended December 31, 2011

SPECIAL HIGHWAY (GAS TAX) FUND

	Current Year		Variance Favorable (Unfavorable)
	Actual	Budget	
Cash Receipts			
State of Kansas gas tax	\$ 23,213	\$ 30,000	\$ (6,787)
Total Cash Receipts	23,213	30,000	(6,787)
Expenditures			
Contractual Service	17,024	50,000	32,976
Capital outlay	3,185	63,049	59,864
Total Expenditures	20,209	113,049	92,840
Receipts Over (Under) Expenditures	3,004	<u><u>\$ (83,049)</u></u>	<u><u>\$ 86,053</u></u>
Unencumbered Cash, January 1	<u>39,793</u>		
Unencumbered Cash, December 31	<u><u>\$ 42,797</u></u>		

The accompanying notes are an integral part of this statement.



City of Cottonwood Falls  
Chase County, Kansas

Statement 3-4

SPECIAL REVENUE FUND  
Statement of Cash Receipts and Expenditures – Actual and Budget  
For the Year Ended December 31, 2011

SPECIAL PARKS & RECREATION FUND

	Current Year		Variance Favorable (Unfavorable)
	Actual	Budget	
Cash Receipts			
Liquor Tax	\$ 1,699	\$ 1,657	\$ 42
Total Cash Receipts	1,699	1,657	42
Expenditures			
Capital Outlay	726	3,975	3,249
Total Expenditures	726	3,975	3,249
Receipts Over (Under) Expenditures	973	<u>\$ (2,318)</u>	<u>\$ 3,291</u>
Unencumbered Cash, January 1	1,055		
Unencumbered Cash, December 31	<u>\$ 2,028</u>		

The accompanying notes are an integral part of this statement.

City of Cottonwood Falls  
Chase County, Kansas

Statement 3-5

SPECIAL REVENUE FUND  
Statement of Cash Receipts and Expenditures  
For the Year Ended December 31, 2011

MUNICIPAL EQUIPMENT RESERVE FUND

	Current Year Actual
Cash Receipts	
Miscellaneous	\$ 0
Operating Transfers	<u>11,667</u>
Total Cash Receipts	<u>11,667</u>
Expenditures	
Capital Outlay	<u>63,932</u>
Total expenditures	<u>63,932</u>
Receipts Over (Under) Expenditures	(52,265)
Unencumbered Cash, January 1	<u>74,286</u>
Unencumbered Cash, December 31	<u>\$ 22,021</u>

The accompanying notes are an integral part of this statement.

City of Cottonwood Falls  
Chase County, Kansas

Statement 3-6

SPECIAL REVENUE FUND  
Statement of Cash Receipts and Expenditures  
For the Year Ended December 31, 2011

SWOPE PARK EQUIPMENT FUND

	Current Year Actual
Cash Receipts	
Donations	\$ 0
State of Kansas	0
	<hr/>
Total Cash Receipts	0
	<hr/>
Expenditures	
Contractual	0
	<hr/>
Total Expenditures	0
	<hr/>
Receipts Over (Under) Expenditures	0
Unencumbered Cash, January 1	<hr/> 7,376
Unencumbered Cash, December 31	<hr/> \$ 7,376

The accompanying notes are an integral part of this statement.

City of Cottonwood Falls  
Chase County, Kansas

Statement 3-7

SPECIAL REVENUE FUND  
Statement of Cash Receipts and Expenditures  
For the Year Ended December 31, 2011

STREETSCAPE FUND

	Current Year Actual
Cash Receipts	
Contributions	\$ 0
Other Receipts	206
Total Cash Receipts	206
Expenditures	
Contractual Service	0
Commodities	350
Total Expenditures	350
Receipts Over (Under) Expenditures	(144)
Unencumbered Cash, January 1	5,730
Unencumbered Cash, December 31	\$ 5,586

The accompanying notes are an integral part of this statement.

City of Cottonwood Falls  
Chase County, Kansas

Statement 3-8

SPECIAL REVENUE FUND  
Statement of Cash Receipts and Expenditures  
For the Year Ended December 31, 2011

COMMUNITY BUILDING EQUIPMENT FUND

	Current Year Actual
Cash Receipts	
Miscellaneous receipts	\$ 0
Total Cash Receipts	0
Expenditures	
Equipment	12
Total Expenditures	12
Receipts Over (Under) Expenditures	(12)
Unencumbered Cash, January 1	97
Unencumbered Cash, December 31	\$ 85

The accompanying notes are an integral part of this statement.

City of Cottonwood Falls  
Chase County, Kansas

Statement 3-9

SPECIAL REVENUE FUND  
Statement of Cash Receipts and Expenditures  
For the Year Ended December 31, 2011

VETERANS MEMORIAL FUND

	Current Year Actual
Cash Receipts	
Contributions	\$ 615
Flag Sales	140
Total Cash Receipts	755
Expenditures	
Contractual Service	0
Commodities	8
Total Expenditures	8
Receipts Over (Under) Expenditures	747
Unencumbered Cash, January 1	8,780
Unencumbered Cash, December 31	\$ 9,527

The accompanying notes are an integral part of this statement.

City of Cottonwood Falls  
Chase County, Kansas

Statement 3-10

SPECIAL REVENUE FUNDS  
Statement of Cash Receipts and Expenditures  
For the Year Ended December 31, 2011

COTTONWOOD FALLS VOLUNTEERS

	Current Year Actual
Cash Receipts	
Donations	<u>\$ 0</u>
Total Cash Receipts	<u>0</u>
Expenditures	
Contractual	<u>0</u>
Total Expenditures	<u>0</u>
Receipts Over (Under) Expenditures	0
Unencumbered Cash, January 1	<u>80</u>
Unencumbered Cash, December 31	<u>\$ 80</u>

The accompanying notes are an integral part of this statement.

City of Cottonwood Falls  
Chase County, Kansas

Statement 3-11

DEBT SERVICE FUND  
Statement of Cash Receipts and Expenditures – Actual and Budget  
For the Year Ended December 31, 2011

BOND AND INTEREST FUND

	Current Year		Variance Favorable (Unfavorable)
	Actual	Budget	
Cash Receipts			
County Tax	\$ 20,360	\$ 20,604	\$ (244)
Other Income	0	0	0
Operating Transfers	0	0	0
Total Cash Receipts	20,360	20,604	(244)
Expenditures			
Principal	15,000	15,000	0
Interest	1,315	1,315	0
Commission and Postage	2	1	(1)
Cash Basis Reserve	0	20,760	20,760
Total Expenditures	16,317	37,076	20,759
Receipts Over (Under) Expenditures	4,043	<u>\$ (16,472)</u>	<u>\$ 20,515</u>
Unencumbered Cash, January 1	16,655		
Unencumbered Cash, December 31	<u>\$ 20,698</u>		

The accompanying notes are an integral part of this statement.



City of Cottonwood Falls  
Chase County, Kansas

Statement 3-12

ENTERPRISE FUND  
Statement of Cash Receipts and Expenditures – Actual and Budget  
For the Year Ended December 31, 2011

SEWER FUND

	Current Year		Variance Favorable (Unfavorable)
	Actual	Budget	
Cash Receipts			
Charges for Services	\$ 44,535	\$ 36,000	\$ 8,535
Other Receipts	0	0	0
Total Cash Receipts	44,535	36,000	8,535
Expenditures			
Personal	22,514	19,400	(3,114)
Contractual	20,799	4,700	(16,099)
Commodities	3,004	316	(2,688)
Capital Outlay	886	69,995	69,109
Total Expenditures	47,203	94,411	47,208
Receipts Over (Under) Expenditures	(2,668)	<u>\$ (58,411)</u>	<u>\$ 55,743</u>
Unencumbered Cash, January 1	45,682		
Unencumbered Cash, December 31	<u>\$ 43,014</u>		

The accompanying notes are an integral part of this statement.

City of Cottonwood Falls  
Chase County, Kansas

Statement 3-13

ENTERPRISE FUND  
Statement of Cash Receipts and Expenditures – Actual and Budget  
For the Year Ended December 31, 2011

SOLID WASTE FUND

	Current Year		Variance Favorable (Unfavorable)
	Actual	Budget	
Cash Receipts			
Charges for Services	\$ 95,199	\$ 70,000	\$ 25,199
Other	0	0	0
Total Cash Receipts	95,199	70,000	25,199
Expenditures			
Personal	6,578	0	(6,578)
Contractual	95,273	70,640	(24,633)
Commodities	88	0	(88)
Capital Outlay	449	41,627	41,178
Total Expenditures	102,388	112,267	9,879
Receipts Over (Under) Expenditures	(7,189)	<u>\$ (42,267)</u>	<u>\$ 35,078</u>
Unencumbered Cash, January 1	<u>36,623</u>		
Unencumbered Cash, December 31	<u>\$ 29,434</u>		

The accompanying notes are an integral part of this statement.

City of Cottonwood Falls  
Chase County, Kansas

Statement 3-14

ENTERPRISE FUND  
Statement of Cash Receipts and Expenditures  
For the Year Ended December 31, 2011

WATER FUND

	Current Year		Variance Favorable (Unfavorable)
	Actual	Budget	
Cash Receipts			
Charges for Services	\$ 163,702	\$ 174,208	\$ (10,506)
Miscellaneous	187	0	187
Total Cash Receipts	<u>163,889</u>	<u>174,208</u>	<u>(10,319)</u>
Expenditures			
General Administration	79,275	90,870	11,595
Production	58,719	33,790	(24,929)
Transmission	<u>56,169</u>	<u>68,119</u>	<u>11,950</u>
Total Expenditures	<u>194,163</u>	<u>192,779</u>	<u>(1,384)</u>
Receipts Over (Under) Expenditures	(30,274)	<u>\$ (18,571)</u>	<u>\$ (11,703)</u>
Unencumbered Cash, January 1	<u>22,724</u>		
Unencumbered Cash, December 31	<u>\$ (7,550)</u>		

The accompanying notes are an integral part of this statement.

City of Cottonwood Falls  
Chase County, Kansas

Statement 4

AGENCY FUNDS  
Statement of Cash Receipts and Cash Disbursements  
For the Year Ended December 31, 2011

Fund	Beginning Cash Balance	Cash Receipts	Cash Disbursements	Ending Cash Balance
Sales Tax	\$ 116	\$ 2,091	\$ 2,076	\$ 131
Customer Deposit	4,088	1,200	517	4,771
Payroll Tax	<u>0</u>	<u>46,302</u>	<u>44,136</u>	<u>2,166</u>
Total	<u>\$ 4,204</u>	<u>\$ 49,593</u>	<u>\$ 46,729</u>	<u>\$ 7,068</u>

The accompanying notes are an integral part of this statement.

City of Cottonwood Falls  
Chase County, Kansas

NOTES TO THE FINANCIAL STATEMENTS  
December 31, 2011

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Financial Reporting Entity

The City of Cottonwood Falls is a governmental entity governed by an elected five-member council and mayor. The City's major operations include public safety and transportation, culture and recreation, and general administrative services. The City also operates three major enterprise activities: a sewer system, a solid waste system, and a water system.

These financial statements present the City of Cottonwood Falls ( the primary government) but do not include the Cottonwood Falls Housing Authority, which is a component unit under Kansas Municipal Audit guidelines.

Fund Accounting

The accounts of the City are organized and operated on the basis of funds, which are used to record the City's financial transactions. A fund is defined as an independent fiscal and accounting entity with a self-balancing set of accounts recording cash and other financial resources, together with all related liabilities and residual equities of balances and changes therein, which are segregated for the purpose of carrying on specific activities or attaining certain objectives in accordance with special regulations, restrictions, or limitations. The following types of funds compromise the financial activities of the City for the year 2011.

Governmental Funds:

General Fund - Fund used as the general operating fund of the City. It is used to account for all financial resources except those required to be accounted for in another fund.

Special Revenue Funds – Funds used to account for the proceeds of specific revenue sources (other than special assessments, expendable trusts, or major capital projects) that are legally restricted to expenditure for specified purposes.

Capital Project Funds – Funds used to account for financial resources for the acquisition or construction of major capital facilities of the City.

Debt Service Funds – Funds used to account for the accumulation of resources for, and the payment of, interest and principal on general long-term debt, and the financing of special assessments which are general obligations of the City.

Proprietary Funds:

Enterprise Funds - Funds used to account for operations (a) that are financed and operated in a manner similar to private business enterprises -- where the intent of the governing body is that the costs (expenses, including depreciation) of providing goods and services to the general public on a continuing basis be financed or recovered primarily through user charges; or (b) where the governing body has decided that periodic determination of revenues earned, expenses incurred, and/or net income is appropriate for capital maintenance, public policy, management control, accountability, or other purposes.

Fiduciary Funds

Trust and Agency Funds – Funds used to account for the collection and disbursement of assets held in trust or as an agent by the City for an individual, a group of individuals, or another government agency.

Statutory Basis of Accounting

The statutory basis of accounting, as used in the preparation of these statutory basis financial statements, is designed to demonstrate compliance with the cash basis and budget laws of the State of Kansas. Cash receipts are recognized when the cash balance of a fund is increased. Expenditures include disbursements, accounts payable, and encumbrances, with disbursements being adjusted for prior year's accounts payable and encumbrances. Encumbrances are commitments related to unperformed (executory) contracts for goods and services, and are usually evidenced by a purchase order or written contract. For an interfund transaction, a cash receipt is recorded in the fund receiving cash from another fund, and an expenditure is recorded in the fund from which the transfer is made.

City of Cottonwood Falls  
Chase County, Kansas

NOTES TO THE FINANCIAL STATEMENTS  
December 31, 2011

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONT)

The City has passed a resolution to waive the requirements of K.S.A. 75-1120a(a). This waiver allows the City to revert to the statutory basis of accounting rather than using generally accepted accounting principles

Departure from Accounting Principles Generally Accepted in the United States of America

The basis of accounting described above results in a financial statement presentation, which shows cash receipts, cash expenditures, cash and unencumbered cash balances, and expenditures compared to budget. Balance sheets that would have shown noncash assets such as receivables, inventories, and prepaid expense; liabilities such as deferred revenue and matured principal and interest payable; and reservations of the fund balance are not presented. Under accounting principles generally accepted in the United States of America, encumbrances are only recognized as a reservation of fund balance; encumbrances outstanding at year-end do not constitute expenditures or liabilities. Consequently, the expenditures as reported do not present the cost of goods sold and services received during the year in accordance with generally accepted accounting principles. General fixed assets that account for the land, buildings, and equipment owned by the municipality are not presented in the financial statements. Also, long-term debt such as general obligation bonds, temporary notes, and compensated absences are not presented in the financial statements.

Use of Estimates

The preparation of financial statements in conformity with the cash basis of accounting requires management to make estimates and assumptions that affect the reported amounts of cash receipts, cash disbursements, cash and unencumbered cash balances, and expenditures at the date of the financial statements. Accordingly, actual results could differ from those estimates.

NOTE 2 - BUDGETARY INFORMATION

Kansas statutes require that an annual operating budget be legally adopted for the general fund, special revenue funds (unless specifically exempted by statute), debt service funds, and enterprise funds. Although directory rather than mandatory, the statutes provide for the following sequence and timetable in the adoption of the legal annual operating budget:

1. Preparation of the budget for the succeeding calendar year on or before August 1st.
2. Publication in local newspaper of the proposed budget and notice of public hearing on the budget on or before August 5th.
3. Public hearing on or before August 15th, but at least ten days after publication of notice of hearing.
4. Adoption of the final budget on or before August 25th.

The statutes allow for the governing body to increase the originally adopted budget for previously unbudgeted increases in revenue other than ad valorem property taxes. To do this, a notice of public hearing to amend the budget must be published in the local newspaper. At least ten days after publication, the hearing may be held, and the governing body may amend the budget at that time. There were no such amendments for this year.

The statutes permit transferring budgeted amounts between line items within an individual fund. However, such statutes prohibit expenditures in excess of the total amount of the adopted budget of expenditures of individual funds. Budget comparison statements are presented for each fund showing actual receipts and expenditures compared to legally budgeted receipts and expenditures.

All legal annual operating budgets are prepared using the statutory basis of accounting in which revenues are recognized when cash is received and expenditures include disbursements, accounts payable, and encumbrances. Encumbrances are commitments by the municipality for future payments and are supported by a document evidencing the commitment, such as a purchase order or contract. Any unused budgeted expenditure authority lapses at year-end.

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NOTES TO THE FINANCIAL STATEMENTS  
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NOTE 2 - BUDGETARY INFORMATION (CONT)

A legal operating budget is not required for capital projects funds, trust and agency funds, and the following special revenue funds: equipment reserve funds, streetscape and veterans memorial. Spending in funds which are not subject to the legal annual operating budget requirement is controlled by federal regulations, other statutes, or by the use of internal spending limits established by the governing body.

NOTE 3 - DEPOSITS AND INVESTMENTS

K.S.A. 9-1401 establishes the depositories which may be used by the City. The statute requires banks eligible to hold the City's funds have a main or branch bank in the county in which the City is located, or in an adjoining county if such institution has been designated as an official depository, and the banks provide an acceptable rate of return on funds. In addition, K.S.A. 9-1402 requires the banks to pledge securities for deposits in excess of FDIC coverage. The City has no other policies that would further limit interest rate risk.

K.S.A. 12-1675 limits the City's investment of idle funds to time deposits, open accounts, and certificates of deposit with allowable financial institutions; U.S. government securities; temporary notes; no-fund warrants; repurchase agreements; and the Kansas Municipal Investment Pool. The City has no investment policy that would further limit its investment choices.

Concentration of credit risk

State statutes place no limit on the amount the City may invest in any one issuer as long as the investments are adequately secured under 9-1402 and 9-1405.

Custodial credit risk – deposits

Custodial credit risk is the risk that in the event of a bank failure, the City's deposits may not be returned to it. State statutes require the City's deposits in financial institutions to be entirely covered by federal depository insurance or by collateral held under a joint custody receipt issued by a bank within the State of Kansas, the Federal Reserve Bank of Kansas City, or the Federal Home Loan Bank of Topeka, except during designated "peak periods" when required coverage is 50%. All deposits were legally secured at December 31, 2011.

At year-end, the carrying amount of the City's deposits, including certificates of deposit, was \$384,054. The bank balance was \$388,729. The difference between the carrying amount and the bank balance is outstanding checks and deposits in transit. Of the bank balance, \$250,000 was covered by FDIC insurance and \$138,729 was collateralized by pledged securities held under joint custody receipts issued by a third-party bank in the City's name. The third-party bank holding the pledged securities is independent of the pledging bank. The pledged securities are held under a tri-party custodial agreement signed by all three parties: the City, the pledging bank, and the independent third-party bank holding the pledged securities. The city held no investments at December 31, 2011.

NOTE 4 - PROPERTY TAXES

The city certifies its' budget to the county clerk annually. Using this certified budget and those of other political subdivisions within the county, the county clerk spreads the annual assessment onto the tax rolls and levies property tax on November 1 of each year. The property tax is payable in two installments. The first installment is due December 20th of the same year, and the second installment is due May 10 of the subsequent year. The county treasurer collects and distributes the property taxes. In accordance with state statutes, property taxes levied during the current year are a revenue source to be used to finance the following year's operations.

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NOTE 5 - COMPENSATED ABSENCES

The City employees earn and accumulate up to 5 days of vacation during the first year of employment, earn 10 days and accumulate 15 days up to 7 years of employment, and earn 15 days and accumulate 15 days thereafter. Employees having accumulated more vacation days before the August 2, 1993 adoption of this policy are allowed to carry forward those days under the prior policy. The City's full-time employees earn up to 12 days per year of sick time and part-time employees earn up to 6 days per year. No employee may accumulate more than 100 days of sick leave and no sick pay is paid upon separation of service. Compensated absence payments are made from the fund that corresponds to the employees duties. No estimate has been made of the total accumulated leave, nor has any been included in these financial statements.

NOTE 6 - LONG-TERM DEBT

The City of Cottonwood Falls issued General Obligation Bonds in 2002 for water plant bond refunding to be retired through calendar year 2012. Annual payments of principal and or interest are due on 3/1 and 9/1 of each year with the final maturity due on 9/1/2012. Payments on these bonds are made from the Bond & Interest Fund.

The City entered into a lease agreement with Cottonwood Valley Bank for the purchase of a Caterpillar Backhoe Loader on November 12, 2009. The city made an initial payment of \$2,850 and fifty-seven monthly payments of \$942.53 are scheduled. The first monthly payment was made in December, 2009. The lease terminates in any budgeted year in which insufficient appropriated funds exist to meet the lease obligation, and the City must return the leased equipment to the lessor. Payments are made from the equipment reserve fund.

The City entered into a lease agreement with Cottonwood Valley Bank for the purchase of a Bobcat Skid-Steer Loader on December 8, 2009. The city made an initial payment of \$2,570 and fifty-seven monthly payments of \$853.79 are scheduled. The first monthly payment was made in January, 2010. The lease terminates in any budgeted year in which insufficient appropriated funds exist to meet the lease obligation, and the City must return the leased equipment to the lessor. Payments are made from the equipment reserve fund.

The City entered into a lease agreement with Cottonwood Valley Bank for the purchase of a 2004 Sterling Trash Truck on April 25, 2012 for \$33,500. Thirty-six monthly payments of \$993.94 are scheduled, beginning May 25, 2012. The lease terminates in any budgeted year in which insufficient appropriated funds exist to meet the lease obligation, and the City must return the leased equipment to the lessor.

Changes in long term liabilities for the year ended December 31, 2011 were as follows:

Issue	Interest Rates	Date of Issue	Amount of Issue	Date of Final Maturity	Beginning Balance	Additions	Reductions/ Payments	Ending Balance	Interest Paid
General Obligation Bonds:									
2002 Water Plant Refunding									
Series 2002	1.7-3.8%	12/15/2002	\$ 412,500	9/1/2012	\$ 35,000	0	\$ 15,000	\$ 20,000	\$ 1,315
Capital Leases Payable:									
Backhoe	4.50%	11/12/2009	51,070	8/12/2014	38,082	0	8,963	29,119	1,404
Skid Steer	4.50%	12/8/2009	46,317	9/5/2014	35,307	0	8,082	27,225	1,310
					<u>\$ 108,389</u>	<u>\$ -</u>	<u>\$ 32,045</u>	<u>\$ 76,344</u>	<u>\$ 4,029</u>



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NOTE 6 - LONG-TERM DEBT (CONT)

Current maturities on long term debt and interest for the next five years and in five year increments through maturity are as follows:

	<u>2012</u>	<u>2013</u>	<u>2014</u>	<u>2015</u>	<u>2016</u>	<u>2017 &amp; thereafter</u>	<u>Total</u>
<b>PRINCIPAL</b>							
General Obligation Bonds	\$ 20,000	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0	\$ 20,000
Capital Leases Payable	<u>28,138</u>	<u>31,395</u>	<u>26,414</u>	<u>3,897</u>	<u>0</u>	<u>0</u>	<u>89,844</u>
Total principal	<u>48,138</u>	<u>31,395</u>	<u>26,414</u>	<u>3,897</u>	<u>0</u>	<u>0</u>	<u>109,844</u>
<b>INTEREST</b>							
General Obligation Bonds	760	0	0	0	0	0	760
Capital Leases Payable	<u>3,167</u>	<u>2,088</u>	<u>700</u>	<u>34</u>	<u>0</u>	<u>0</u>	<u>5,989</u>
Total interest	<u>3,927</u>	<u>2,088</u>	<u>700</u>	<u>34</u>	<u>0</u>	<u>0</u>	<u>6,749</u>
Total Principal and Interest	<u>\$ 52,065</u>	<u>\$ 33,483</u>	<u>\$ 27,114</u>	<u>\$ 3,931</u>	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 116,593</u>

NOTE 7 - DEFINED BENEFIT PENSION PLAN

Plan description The City of Cottonwood Falls participates in the Kansas Public Employees Retirement System (KPERS), a cost sharing multiple-employer defined pension benefit plan as provided by K.S.A. 74-4901, *et seq.* KPERS provides retirement benefits, life insurance, disability income benefits, and death benefits. Kansas law establishes and amends benefit provisions. KPERS issues a publicly available financial report that includes financial statements and required supplementary information. That report may be obtained by writing to KPERS (611 S. Kansas, Suite 100, Topeka, KS 66603) or by calling 1-888-275-5737.

Funding policy K.S.A. 74-4919 establishes the KPERS member-employee contribution rate at 4% or 6% of covered salary. The employer collects and remits member-employee contributions according to the provisions of section 414(h) of the Internal Revenue Code. State law provides that the employer contribution rate be determined annually based on the results of an annual actuarial valuation. KPERS is funded on an actuarial reserve bases. State law sets a limitation on annual increases in the contribution rates for KPERS employers. The employer rate established for 2011 was 7.74% with a 1% reduction for April through June. The City's contributions to KPERS for the years ending December 31, 2011, 2010, and 2009 were \$12,564, \$11,764, and \$8,898, respectively, equal to the required contributions for each year.

NOTE 8 – OPERATING LEASES

The City entered into an agreement to lease the Santa Fe well from Robin & Rebecca Roberts. The annual lease amount is \$1,000 per year effective January 1, 2007. The five year lease term expired on December 31, 2011 and has not been renewed.

The City entered into a twenty-year lease agreement for an easement regarding the road to the water plant with Elmo Starkey for \$750 per year in November 1997.

The following is a schedule of the future operating lease payments due to Elmo Starkey:

<u>Year</u>	<u>Amount Due</u>
2012	750
2013	750
2014	750
2015	750
2016	750
2017	750

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NOTE 9 – FUND TRANSFERS

During 2011, the city transferred monies between funds as allowed by applicable Kansas statutes. The following schedule details transfers made in 2011.

<u>Transferred from:</u>	<u>Transferred to:</u>	<u>Statute</u>	<u>Amount</u>
General	Equipment Reserve	12-1,117	\$ 11,667

NOTE 10 – COMPLIANCE FINANCE-RELATED LEGAL AND CONTRACTUAL PROVISIONS

References made herein to the statutes are not intended as interpretations of law, but are offered for consideration of the Director of Accounts and Reports and legal representatives of the municipality.

The Water Utility showed a negative unencumbered cash balance at year end of (\$7,550), which is in violation of K.S.A 10-1113. The actual cash balance showed a positive balance but after recording accounts payable and encumbrances, as required by the Kansas statutory basis of accounting, the unencumbered cash fund balance was negative.

The Water Utility expenditures were in excess of budgeted limits in violation of K.S.A. 79-2935.

Management is not aware of any other items of noncompliance with Kansas statutes.

NOTE 11 – OTHER POST EMPLOYMENT BENEFITS

As provided by K.S.A. 12-5040, the City allows retirees to participate in the group health insurance plan until age 65. While each retiree pays the full amount of the applicable premium, conceptually, the City is subsidizing the retirees because each participant is charged a level premium regardless of age. However, the cost of this subsidy has not been quantified in these financial statements.

Under the Consolidated Omnibus Budget Reconciliation Act (COBRA), the City makes health care benefits available to eligible former employees and eligible dependents. Certain requirements are outlined by the federal government for this coverage. The premium is paid in full by the insured. There is no cost to the City under this program.

NOTE 13 – RISK MANAGEMENT

The city is exposed to various risks of loss related to torts: theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. In 2011, the city was unable to obtain worker's compensation insurance at a cost it considered to be economically justifiable. For this reason, the city joined together with other cities in the State to participate in the Kansas Municipal Insurance Trust (KMIT), a public entity risk pool currently operating as a common risk management and insurance program for participating members.

The city pays an annual premium to KMIT for its worker's compensation insurance coverage. The agreement to participate provides that the KMIT will be self-sustaining through member premiums and will reinsure through commercial companies for claims in excess of a specified amount for each insured event. Additional premiums may be due if total claims for the pool are different than what has been anticipated by KMIT management.

The city continues to carry commercial insurance for all other risks of loss, including property and liability insurance. There were no significant reductions in coverage from coverage in place in prior years.

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NOTE 14 – RELATED PARTY

On July 5, 2011 the City of Cottonwood Falls purchased two trucks, for use in a city operated trash utility, from Wichita Kenworth Inc. at a total cost of \$51,195. The Mayor of the City of Cottonwood Falls, Mike Swartz, is an employee of Kenworth and was the salesman of record for this purchase.

NOTE 15 – SUBSEQUENT EVENTS

The City of Cottonwood Falls determined that it would be cost effective to operate its trash utility rather than contract it out to another company as it has done in the past. The city invested in two trash trucks, poly carts and dumpsters and took over the operation of the trash pickup in the city in May of 2012.

The City of Cottonwood Falls has approved a water line improvement project in the city at an estimate cost of \$1.6 million. The city has applied for a \$500,000 Community Development Block Grant and a \$1.1 million loan from the Kansas Department of Health & Environment to finance the improvements. Final approval on the financing has not yet been granted. The City anticipates beginning the project in 2013.

The City of Cottonwood Falls joined together with the City of Strong City and the Rural Water District No. 1 to form Public Wholesale Water Supply District No. 26. The purpose of the District is to produce, treat, transport, distribute, and sell an adequate source of water wholesale to its members, including the City of Cottonwood Falls. The District is planning a capital project at an estimated cost of \$5,270,000, to construct the necessary facilities and equipment to fulfill this purpose. The District is currently awaiting approval on grants and loans to finance this project.

The City of Cottonwood Falls entered into an agreement for the option to lease its water wells to the Public Wholesale Water Supply District No. 26 for a sum of \$1.00 and other good and valuable consideration for a term of 40 years or so long as the District provides water from the wells. The agreement commences when the District is capable of receiving water into its lines and producing and treating water in a water treatment plant.